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Tuesday, September 19, 2006

Blown down in the wind: property rights and the public interest doctrine

The public interest (or public use) doctrine has been widely used in U.S. law in areas ranging from constitutional law (including the Takings Clause, substantive due process, and the First Amendment) to bankruptcy law and the regulation of public utilities, telecommunications, and transportation businesses in particular as well as of business generally. But this doctrine has been radically changed in form over the years, until today it is a only a mockery of its original form.

From its origins in the medieval doctrines of seisin and feudal service, as applied to private rights to exercise police powers or to charge taxes or tolls, it was extended to apply to franchises and monopolies in general. During the New Deal, the idea was preposterously expanded to justify even the arbitrary and discriminatory regulation of every kind of property.

In medieval times governmental jurisdiction was property. Like other property, it was either derived by title ultimately from the king or by long use (prescription). Like other property, it was governed by the doctrine of seisin, or active and notorious possession. Often property , including land, entailed, as a matter of obligation specified in charter (the deed under which property was conditionally transferred) or as a matter of custom, obligations such as military service, rent, or maintaining or using the property. In the context of a franchise involving police powers, the doctrine of "non-user," justified as either seisin or implied feudal obligation, often imposed certain procedural obligations -- for example to exercise the police power against lawbreakers and to respect the right of trial by jury. The non-user doctrine was, however, controversial, and owners of these intangible properties argued that their franchises, even franchises to collect taxes and tolls or exercise police powers, were purely private property for their private use.

In 1237 King Henry II argued, in a letter to the Abbott of Peterborough, that his grant to the abbott of local police powers was conditional on their being exercised:

> Since we ordered all the bailiffs in our realm to see that watches were kept by night against the disturbers of our peace and commanded that the holders of liberties [i.e. franchises] should see that this was observed in their liberties, we marvel greatly that you in your liberty of Peterborough have allowed homicide and theft to be committed, and have taken no steps to keep our peace...We enjoin you therefore that, as you wish to retain your liberty, you take care to deal with malefactors and peace breakers, so that it may appear that you are a lover of peace, and that we may not have to lay our hands upon your liberty because you have failed.

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Nick Szabo

"A premier thinker about history, law and economics, and the lessons they have for security." -- Adam Shostack, Emergent Chaos

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A more recent case that illustrated this debate is *Att.-Gen. v. Newdegate* (King's Bench 1519). This case was to determine whether the franchises of "infangthief" and "outfangthief" that had been deeded by the king to Newdegate for his manor was forfeit back to the king due to "non-user." "Infangthief" was the right to hang those who had committed a theft on the land and caught red-handed on the land, and "outfangthief" was the right to hang such a thief even if caught red-handed elsewhere.

According to a report of the case, "the king's attorney showed that [Newdegate] had not used it, and had also misused it, for he did not have gallows..." Newdegate's attorney lamely explained that "his gallows were blown down in the wind," but over a year had gone by and they were still down. He argued that whatever the reason the gallows were blown down was irrelevant because "non-user is neither a forfeiture nor finable because this is a liberty [franchise] granted to him which he may use as he wishes, and it is for his own advantage." Another words, he was arguing -- and it was a plausible argument at the time -- that even a function we now consider a core governmental function was purely a matter of private property. Even a police force and a court did not in this view entail enough public interest to justify common law regulation.

However, Chief Justice Fyneux held that "this leet [i.e. the private court] is granted for the common wealth as well as for the benefit of the party [owner], and it must be used or else it is forfeit." Whereas in previous centuries this kind of forfeiture proceeding, called a *quo warranto,* was considered merely a dispute over title to the franchise as either the king's private property or the current operator's private property, now the franchise of monopoly police power over an area was considered to have a pubic interest. It was this public interest, not an implied feudal obligation to the king as grantor of the franchiise, that now justified common law obligations and restrictions on the use of a police powers franchise.

In the late 17th century, Lord Chief Justice Hale, in his treatise *De Portibus Maris (Concerning the Gates to the Sea)* applied this doctrine to franchises to take taxes or tolls. All rights to charge taxes or tolls were originally the property of the king (the king's prerogative), but like the king's jurisdiction it was often granted or owned by prescription by other parties in the form of a franchise. Hale discussed the issue of what kind of commercial enterprise constituted taking a "toll," and thus required an intangible property right -- a franchise -- on top of the personal and real property of the enterprise in order to legally operate the enterprise. If the price was a toll, the enterprise was performed under franchise with a public interest, and thus would be regulated by the common-law franchise doctrines of non-user (the requirement of continual use for the public) and that the rate charged be reasonable.

Besides toll-roads and bridges, for Hale toll-taking included being the sole operator of a port facility such as a wharf or a set of cranes, or the operator of the sole ferry in an area. Hale justified this scope of public interest by citing the Roman idea of *juris publica,* under which the emperor, rather than local authorities or private parties (*juris privati*) had jurisdiction over the ocean shoreline.

These monopolistic situations with high avoidance costs were, however, still plausible variants of the right to collect taxes or tolls. According to Hale, when such a monopoly was either expressly a franchise granted by the king or was a toll-taking monopoly owned by prescription, the owner of the monopoly had to charge a reasonable rate. Hale describes such a franchise as "a right privilege, that no man may set up a common ferry for all passengers without a prescription time out of mind or a charter from the king. He may make a ferry for his own use or the use of his family, but not for the common use of all the king's subjects passing that way; because it doth in consequent tend to a common charge, and is become a thing of public interest and use, and every man for his passage pays a toll, which is a common charge, and every [such] ferry ought to be under a public regulation, viz., that it give attendance at due times, keep a boat in due order, and take but reasonable toll; for if he fail in these he is finable." As long as the property right is equivalent to the monopoly of taking a toll on a road, the property is "affected with a public interest." This interest, however, terminates if competition arises. If the situation is not or is no longer the equivalent of taking the toll -- i.e. if it does not involve "all" the king's subjects who travel that way -- freedom of contract (i.e. property rights in motion) must govern:

> A man, for his own private advantage, may, in a port or town, set up a wharf or crane, and may take what rates he and his customers can agree for cranage, wharfage, housellage, pesage; for he doth no more than is lawful for any man to do,

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> viz., makes the most of his own. If the king or subject have a public wharf, unto which all persons that come to that port must come and unlade or lade their goods as for the purpose, because they are the wharves only licensed by the king, or because there is no other wharf in that port, as it may fall out where a port is newly erected, in that case there cannot be taken arbitrary and excessive duties for cranage, wharfage, pesage, &c.; neither can they be enhanced to an immoderate rate, but the duties must be reasonable and moderate, though settled by the king's license or charter. For now the wharf and crane and other conveniences are affected with a public interest, and they cease to be *juris privati* only; as if a man set out a street in new building on his own land, it is now no longer bare private interest, but is affected by the public interest.

Up to here the public interest was required to justify a common law restriction on a franchise. In medieval and Renaissance times, on rare occassions Parliamentary statutes, and much more commonly local lords and guilds, regulated property in motion, with various oppressive or economically dubious laws that fixed prices, set maximum wages, and the like. These regulations were not considered part of the common law and were not justified in terms of the public interest doctrine. However, in the U.S. the Fourteenth Amendment was commonly held by legal scholars and judges to apply common law restrictions to statutory law, and that included restricting regulation of private property by the public interest doctrine as it had been explicated by Hale. The Waite, Peckham, and Taft Courts all agreed that the public interest doctrine restricted the ability both state and federal legislatures to regulate private property, but in the process of applying the doctrine in this way the Supreme Court ended up stretching it beyond all recognition, until it just broke.

This conflict between the legislative desire to regulate property and the common law restrictions incorporated in the Fourteenth Amendment came to a head little more than a decade after the ratification of that Amendment. The common law doctrine of public interest was applied to restrict legislation, but it was even in the first case stretched to allow legislation that was far from regulation of any sort of private police power or toll-taking.

In *Munn v. Illinois* (US. Supreme Court 1877) the public interest doctrine was rather dubiously extended to a set of grain elevator situated near a major railroad hub in Chicago. These elevators sorted and stored grain and thus played an important role in the shipment and trading of grain. Their construction and operation had greatly expanded the ability of Midwest U.S. farmers to market their products, but now the farmers had complained about the high prices charged and successfully lobbied, via a political lobbying group called the Grangers, for Illlinois to regulate the rates charged by the elevators for storing grain.

Munn's elevators did not comprise all (or even most) of the elevators near the hub. There were several companies operating such elevators, albeit they had been accused of collusion. Nevertheless, there is an economic rationale for extending the public interest doctrine to what Professor Richard Epstein calls network companies -- companies like public utilities and railroads. Given the exclusive contracts between railroads and the grain elevators, and anti-scompetitive collusion between the elevator companies itself, the network doctrine could plausibly be further extended from the railroads to the elevators. Whether or not it was justifiable on policy grounds, *Munn* was a radical redefinition of the public interest doctrine. No longer was the doctrine confined to performing governmental functions, i.e. running courts and police forces and collecting taxes and tolls, when the rights to conduct such activities were privately owned. Now the public interest doctrine applied to purely commercial enterprises that were not purely competitive but were associated with some uncompetitive practices or outcomes.

The network or anticompetitive theory lasted for a little over seventy years, but it was easy for courts to extend this doctrine, since no commercial enterprise is purely competitive. Indeed, as Professor Epstein has described, the Progressive and pro-New Deal judges thought highly regulated monopolies or cartels were the ideal form of business for most sectors of the economy. In *Nebbia v. New York* (U.S. Supreme Court 1934) Justice Roberts declared that the public interest doctrine justified almost arbitrary and discrimanatory regulation of property:

> The court has repeatedly sustained curtailment of enjoyment of private property, in the public interest. The owner's rights may be subordinated to the needs of other private owners whose pursuits are vital to the paramount interests of

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> the community. The state may control the use of property in various ways; may prohibit advertising bill boards except of a prescribed size and location, or their use for certain kinds of advertising; may in certain circumstances authorize encroachments by party walls in cities; may fix the height of buildings, the character of materials, and methods of construction, the adjoining area which must be left open, and may exclude from residential sections offensive trades, industries and structures likely injuriously to affect the public health or safety; or may establish zones within which certain types of buildings or businesses are permitted and others excluded. And although the Fourteenth Amendment extends protection to aliens as well as citizens, a state may for adequate reasons of policy exclude aliens altogether from the use and occupancy of land [citations omitted].

In terms of what local lords and legislatures had actually regulated over the course of history this was accurate. In the context of the history of franchise law, on which Hale's public interest doctrine was based, and which the Fourteenth Amendment had been held to incorporate, but which Justice Roberts had forgotten, this interpretation of the public interest doctrine was absurd. "Public interest" now refered, not to coercive police powers, not to toll-taking, not to toll-like monopolies, not to businesses with network externalities, but simply to the ubiquitous condition of scarcity, used in *NBC v. U.S.* (U.S. Supreme Court 1943) even to deny First Amendment claims against content-related FCC regulations:

> The facilities of radio are limited and therefore precious; they cannot be left to wasteful use without detriment to the public interest.

The Waite Court's application of the doctrine to network-like businesses generally, including not just railroads but also semi-monopolistic depots standing beside railroads, had already stetched the doctrine well beyond toll-taking proper. Now the doctrine was simply smashed down altogether by the New Deal hurricane.

Posted by Nick Szabo at 6:59 PM

4 comments:

Richard Maxwell Underwood said...

I've been reading your blog for about

six months, and I highly value it.
I'm using it to round out my general
education, which is woefully deficient in knowledge of the law.

This entry is especially useful and interesting to me. ditto the entry in June on jurisdiction as property, which I had no idea about before reading your blog.

In fact, all your entries last four
months on the common-law tradition have been wonderful.

9:33 PM

Nick Szabo said...

This is great feedback to hear, thanks!

12:45 AM

Anonymous said...

Thanks for the information! (Business franchise information)

1:35 AM

Anonymous said...

This information is very useful for me, thank you! I've got a blog with business franchise information. Maybe you will also find something useful for you.

1:37 AM

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